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CONFIDENTIAL

13 January 2012

By hand

Companies Bill Team
Financial Services and the Treasury Bureau
Government of the Hong Kong Special Administrative Region
15th Floor, Queensway Government Offices
66 Queensway, Hong Kong

Dear Sirs,

Companies Bill - Consultation Paper on the Qualifying Criteria for Private Companies to Prepare Simplified Financial and Directors' Reports

We are pleased to provide our comments on the captioned Consultation Paper. Capitalized terms used in this letter have the same meaning as ascribed to them in the Consultation Paper.

We acknowledge that the majority of private companies in Hong Kong are owner-managed and the users of their financial reports are mainly owners, the tax authority and lenders and their financial reports are considered to have a lesser degree of public interest. We support the government's initiative to introduce an automatic mechanism to qualify private companies and holding companies of groups of private companies (except for companies that are specifically prohibited under the Companies Bill) meeting certain size criteria for simplified reporting.

We understand that the extant SME-FRF&FRS, the applicable accounting framework and standard for simplified reporting, are essentially developed for SMEs on a single company basis. Unlike the IFRS for SMEs which has been widely used internationally by SMEs, the SME-FRS does not provide specific guidance and requirements on issues such as business combinations, investments in associates and joint ventures, financial instruments and statement of cash flows. We believe that issues relating to consolidated financial statements would be addressed if the use of SME-FRF&FRS is to be extended to groups. However, we have reservations on whether the revised

SME-FRF&FRS are suitable for large private companies/groups with sizable operations, which could have more complex transactions, arrangements or structures, and their financial reports are likely to have a higher degree of public interest.

Furthermore, as an international financial center, it is important for Hong Kong to reinforce and promote quality financial reporting. Therefore, we do not agree with one of the proposed options, which allows the (majority of) members of private companies of any size to opt for the use of the SME-FRF&FRS. We believe large private companies/groups should adopt either the HKFRS or the HKFRS for Private Entities, which is based on IFRS for SMEs and is a more robust financial reporting standard.

Our views on the three options set out in paragraphs 11 to 21 of the Consultation Paper are set out below:

Option 1 (Private companies/the holding companies of groups meeting the size criteria can automatically qualified for simplified reporting. Large private companies/groups cannot opt in.)

We agree with this option. We have concerns that the SME-FRF&FRS might not be suitable for large private companies/groups. In addition, there is a need to maintain quality financial reporting in Hong Kong and accordingly we support the proposal that large private companies/groups cannot opt in.

We note that the HKICPA is concurrently carrying out a consultation on the eligibility for the use of SME-FRF&FRS and is proposing to revise the size criteria. We would advise the government to consider the observations and comments drawn from that consultation before finalizing the size criteria.

Option 2 (Private companies/the holding companies of groups meeting the size criteria can automatically qualify for simplified reporting. Large private companies/groups can opt in if members holding at least 75% of the voting rights so resolve and no other member objects.)

We disagree with this option. We believe that large private companies/groups which failed the size criteria should not be allowed to adopt simplified financial reporting notwithstanding the approval of their members. As explained above, we consider that large private companies are normally engaged in more sizable operations and their financial reports have a higher degree of public interest. They should be subject to a more robust financial reporting framework.

Option 3 (Private companies/the holding companies of group meeting the size criteria can automatically qualify for simplified reporting. Large private companies/groups can opt in if members holding at least 75% of the voting rights so resolve and no other member objects, subject to their size not exceeding a higher threshold.)

We understand this option seeks to strike a balance between maintaining an appropriate level of transparency and reducing the compliance costs for large private companies/groups. However, we believe that as long as an appropriate higher threshold has been set (as in option 1), an automatic qualifying mechanism would help save administrative costs.

The above comments are submitted for your consideration. If you have any questions on these comments, please do not hesitate to contact the undersigned at 2236 6001.

Yours faithfully,



P.M. Kam
Chief Executive Officer
Financial Reporting Council